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INFO RUEHBO/AMEMBASSY BOGOTA 7759
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RUMIAAA/HQ USSOUTHCOM MIAMI FL
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HQ SOUTHCOM ALSO FOR POLAD
TREASURY FOR MMALLOY
NSC FOR JSHRIER
COMMERCE FOR 4431/MAC/WH/MCAMERON

E.O. 12958: DECL: 04/22/2018
TAGS: ECON EFIN VE
SUBJECT: BRV ANNOUNCES 3 BILLION USD BOND ISSUANCE TARGETED
AT IMPORTERS

REF: A. CARACAS 475

¶B. CARACAS 376
¶C. CARACAS 190
¶D. 2007 CARACAS 2186

Classified By: Acting Economic Counselor Shawn Flatt for reasons 1.4 (b
) and (d).

More Dollars (or Rather Bonds) For Bs

¶1. (U) The Ministry of Finance (MoF) announced on April 21 a USD 3 billion sovereign debt issuance. The issuance is composed of two "Sovereign International Bonds" (SIBs), dollar-denominated bonds maturing in 2023 (9 percent coupon) and 2028 (9.25 percent coupon), with each representing 50 percent of the issuance. As with several recent issuances (ref D), the bonds are payable in bolivars (Bs) at the official exchange rate of 2.15 Bs/USD. The bond price, announced April 22, is 115 percent of face value. Local financial consultants anticipate that the "implicit exchange rate" obtained by purchasing the bonds in bolivars will be roughly 2.9 Bs/USD. (Note: In order to calculate the implicit rate, one has to determine the dollar price the bond can be sold for on the secondary market and factor in commission costs and taxes as well. End note.) Offers are due April 24 and the results, including the adjudication method that will be used to decide which offers are accepted, will be announced April 28.

A New Definition of "Productive Companies"

¶2. (SBU) As the Minister of Finance had previously suggested (ref A), up to 50 percent of the issuance will be made available to selected importers, specifically, according to the prospectus, to "productive companies" that are registered with CADIVI (the BRV's exchange control board) and whose "social purpose implies the development of productive activities in the sectors of food, health, and capital goods." The prospectus further claims that the purchase of SIBs will have no impact on companies' "procedures" for soliciting foreign exchange with CADIVI. The process by

which eligible "productive companies" will be determined, however, is not transparent, nor is it clear whether the purchase of SIBs by a given company will place its pending CADIVI requests in jeopardy. The remainder of the issuance will be allocated to individuals and legal entities domiciled and/or resident in Venezuela. An MoF press release states that the two component bonds will not be registered under the U.S. Securities Act of 1933, noting that they will only be offered for sale outside the U.S.

Continuing to Target the Parallel Rate

¶3. (C) The SIB issuance represents an expected step in the BRV's strategy to bring down the parallel rate for dollars and thereby, the government hopes, reduce inflationary pressures (ref B). Nelson Merentes (strictly protect), a former Minister of Finance under President Chavez who is still closely connected to the BRV, told Econoff on April 21 that the BRV hopes to drive the parallel rate down to between 2.8 and 3 Bs/USD by July. (Note: The parallel rate is currently at about 3.4 Bs/USD. End note.) Acknowledging that using new debt issuances to supply dollars to the parallel market was not a sustainable strategy given the limited demand for additional Venezuelan debt in secondary markets, he hinted that future supply of dollar-denominated instruments would come from the National Development Fund (FONDEN), although using different instruments than the "structured notes" sold earlier this year (ref C). (Note: Prices of existing Venezuelan bonds dropped on April 21 after the announcement, confirming the limited demand for additional Venezuelan debt. End note.)

Comment: Yet Another Parallel Institution?

¶4. (C) Comment: What is new about this bond issuance is not its targeting of the parallel rate but rather its allocation to importers. As such, it may herald the beginning of an unofficial dual exchange rate strategy whereby CADIVI allocates a certain amount of dollars to importers at the official rate and the MoF allocates an additional amount of dollar-denominated assets to importers at another exchange rate in between the official rate and the parallel rate. If so, it represents another instance where the BRV creates a parallel institution (MoF allocations of financial instruments) to try to address problems with a failing institution (CADIVI allocations of hard currency; more septel) without addressing the root causes of the problem (prolonged exchange controls and an overvalued currency). This new mechanism stands little chance of being efficient because, as with CADIVI, allocation depends on BRV discretion rather than the market. Furthermore, given the bonds' fungibility, there is no economic reason that allocating them to importers of certain goods will increase imports of those goods, as the importer might choose to make a quick profit by reselling the bonds for bolivars on the parallel market rather than using them to finance imports. Finally, calling the importers who receive these bonds "productive companies" is a classic example of how words often trump reality in the BRV.
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